

Message Text

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ACTION EUR-25

INFO OCT-01 EA-11 ADP-00 EURE-00 CIAE-00 DODE-00 PM-09

H-02 INR-09 L-03 NSAE-00 NSC-10 PA-03 RSC-01 PRS-01

SS-14 USIA-12 AID-20 EB-11 CIEP-02 SAL-01 STR-08

OMB-01 CEA-02 IO-12 COME-00 FRB-02 TRSE-00 XMB-07

OPIC-12 LAB-06 SIL-01 RSR-01 INRE-00 /187 W

----- 045277

P R 281828 Z MAR 73

FM AMEMBASSY LONDON

TO SECSTATE WASHDC PRIORITY 0092

INFO AMEMBASSY BONN

USMISSION EC BRUSSELS

AMEMBASSY PARIS

USMISSION OECD PARIS

AMEMBASSY ROME

AMEMBASSY TOKYO

C O N F I D E N T I A L SECTION 01 OF 02 LONDON 03679

NOFORN PASS TREASURY; FRB

E. O. 11652: GDS

TAGS: EFIN, UK

SUBJECT: CURRENT INTERNATIONAL FINANCIAL SITUATION
(C- EB-57203)

REF: STATE 54202

1. BELIEVE THAT SOME OF THE QUESTIONS IN REFTEL (IN PARTICULAR, PARAS 2 AND 3) HAVE LIMITED APPLICABILITY INDEPENDENTLY FROM OTHER CURRENCIES.
 2. RE PARA 4 REFTEL, VIEWS OF UK BANKERS AND OFFICIALS RANGE FROM CAUTIOUS OPTIMISM TO OUTRIGHT SKEPTICISM. IN THE PRIVATE SECTOR, THERE IS NO FIRM BELIEF THAT THE DOLLAR DEVALUATION AND THE COMMON EC FLOAT PROVIDE THE
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CORRECT ANSWER. MOST OFFICIALS AND BUSINESSMEN HOPE THAT THE CRISIS IS FINALLY OVER. CONTINUED SPECULATION IN GOLD AT A PRICE AROUND \$90 IS, HOWEVER, A REMINDER THAT THERE ARE WIDELY EXPRESSED FEARS NOT ONLY OF CURRENCY INSTABILITY BUT ALSO OF WORLD- WIDE INFLATIONARY TRENDS.

3. THE US PERFORMANCE, INCLUDING THAT OF UNDER SECRETARY VOLCKER DURING THE WEEKEND LEADING TO FEBRUARY 12 DEVALUATION, HAS BEEN PRAISED IN THE UK. THE PRESS COMMUNIQUE OF THE G-10 MEETING HELD PRECIPITATED ENOUGH; SOME CITE A 255 YEN TO THE DOLLAR RATE AS APPROPRIATE. THEY ALSO CONSIDER THAT THE SWISS FRANC RATE MAY HAVE GONE TOO HIGH. LOOKING AHEAD, THEY SEE CONTINUED INDEPENDENT FLOATING OF THE POUND INTO THE INDEFINITE FUTURE, UNLESS THE MAJOR POINTS SPELLED OUT IN LONDON-2718 ARE ACCEPTED BY THE UK'S PARTNERS IN THE EC.

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ACTION EUR-25

INFO OCT-01 EA-11 ADP-00 EURE-00 CIAE-00 DODE-00 PM-09

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AMEMBASSY PARIS
USMISSION OECD PARIS

AMEMBASSY ROME
AMEMBASSY TOKYO

C O N F I D E N T I A L SECTION 02 OF 02 LONDON 03679

NOFORN PASS TREAS

DOES CONTAIN AN ELEMENT OF DISCIPLINE INASMUCH AS EACH
5 PERCENT DEVALUATION INCREASES THE RETAIL PRICE LEVEL
BY ROUGHLY 1 PERCENT. THE EXTERNAL EXCHANGE RATE CANNOT
BE ALLOWED TO DRIFT DOWNWARDS WITH IMPUNITY; THERE ARE
DOMESTIC PRICE EFFECTS AS WELL AS THE INTERNATIONAL
TERMS OF TRADE EFFECTS ON THE BALANCE OF PAYMENTS. THE
LABOR PARTY HAVE MADE CLEAR THAT THEY WILL NOT OPPOSE
CONTINUED FLOATING IN THE PRESENT CIRCUMSTANCES. THERE
IS A WIDELY HELD BELIEF IN THE PRIVATE SECTOR THAT IF
BRITAIN WERE TO JOIN THE COMMON EC FLOAT, IT WOULD HAVE
TO BE AT A LOWER STERLING EXCHANGE RATE THAN CURRENTLY
QUOTED IN INTERNATIONAL MARKETS.

5. THE UKTREASURY IS WATCHING THE OPERATION OF THE SNAKE
WITH INTEREST AND SOME SKEPTICISM, WONDERING ESPECIALLY
WHAT THE FRENCH REACTION WILL BE IF THE FRANC WINDS UP
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AT THE BOTTOM OF THE SNAKE WITH ATTENDANT LOSSES TO
FRENCH RESERVES.

6. BRITISH GOVERNMENT OFFICIALS AND PRIVATE INDUSTRY
FINANCIAL OFFICIALS GENERALLY CONSIDER THAT THE JAPANESE
YEN HAS NOT APPOINT STATEMENT WHICH
WOULD DEFINE THE MANNER IN WHICH HUNGARY WAS PUT IN
ABEYANCE; (2) IF AGREEMENT WERE NOT POSSIBLE ON A SINGLE
JOINT STATEMENT, THERE COULD BE COMPLEMENTARY STATEMENTS
BY HUNGARY AND BY THE WESTERN SIDE DEFINING POSSIBLE
MODES OF FUTURE HUNGARIAN PARTICIPATION; (3) ALTERNA-
TIVELY, THERE COULD BE AGREEMENT TO LIST ALL 19 PARTI-
CIPANTS, 11 DIRECT PARTICIPANTS, A FORMULA FOR POSSIBLE
ENLARGEMENT OF THIS GROUP AND A LIST OF 7 SPECIAL PAR-
TICIPANTS. IN ADDITION, ALLIED REPS REVIEWED IN DETAIL
CONCEPTS WHICH COULD BE EMBODIED IN EITHER A SINGLE AGREED
STATEMENT OR TWO COMPLEMENTARY STATEMENTS, DRAWING FOR
THIS PURPOSE UPON POSSIBLE STATEMENTS DEVELOPED IN AD HOC
GROUP.

3. EASTERN REPS WHOSE ATTITUDE WAS RECEPTIVE, QUESTIONED
ALLIED SPOKESMEN EXTENSIVELY ON POSSIBLE CONTENT OF
STATEMENTS, AND ON RELATIONSHIP BETWEEN STATEMENTS AND
AN AGREED PROCEDURES PAPER. AT CONCLUSION, THEY SAID
THAT THEY WOULD LIKE TO STUDY THE NEW IDEAS PUT FORWARD
IN THIS SESSION, AND FORMULATE CONSIDERED REACTIONS AND

QUESTIONS FOR DISCUSSION ON NEXT OCCASION. AS A PRE-LIMINARY REACTION, HOWEVER, THEY WISHED TO NOTE THEIR IMPRESSION THAT ALLIED THINKING CONTINUED TO BE A WAY FOR WESTERN SIDE TO GAIN POSSIBILITY OF RAISING HUNGARIAN PARTICIPATION IN THE FUTURE WITHOUT CREATING A SIMILAR BASIS FOR EAST TO ADDRESS ITALIAN PARTICIPATION, BUT THAT DIALOGUE SHOULD BE CONTINUED. ALLIED REPS REITERATED THAT ROLE OF ITALY HAD BEEN DETERMINED, AND WAS NOT PRODUCTIVE SUBJECT FOR DISCUSSION. GROUP AGREED TENTATIVELY TO MEET MORNING OF MARCH 30 AT HUNGARIAN EMBASSY. END SUMMARY.

4. MARCH 28 DISCUSSION ON THE HUNGARIAN ISSUE TOOK PLACE
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IN NETHERLANDS EMBASSY, WITH US AND NETHERLANDS REPS PRESENT ON THE ALLIED SIDE, AND WITH KHLESTOV, KVITSINSKIY AND TIMERBAYEV REPRESENTING THE USSR AND USTOR AND PETRAN, HUNGARY. NETHERLANDS REP WELCOMED EASTERN REPS, NOTED THAT PURPOSE OF DISCUSSION WAS TO SEEK A NEUTRAL SOLUTION TO THE HUNGARIAN PROBLEM AND SUGGESTED THAT PARTICIPANTS LEAVE ASIDE FOR THE MOMENT PAST HISTORY OF THIS ISSUE AND THE PREVIOUS ARGUMENTS ON BOTH SIDES AND CONCENTRATE INSTEAD ON PRACTICAL WAYS TO FIND A NEUTRAL SOLUTION. HE ASKED WHETHER IN THE INTERVAL SINCE THE LAST DISCUSSION, THE EASTERN REPRESENTATIVES HAD DEVELOPED ANY NEW IDEAS WHICH THEY COULD PUT FORTH.

5. KHLESTOV, READING FROM NOTES, REPLIED THAT HE WOULD LIKE TO UNDERScore AT THE OUTSET THE VIEW OF HUNGARY AND THE USSR THAT THE QUESTION OF PARTICIPANTS AND DECISION-MAKING RELATING TO A CONFERENCE ON THE REDUCTION OF ARMED FORCES AND ARMAMENTS IN CENTRAL EUROPE MUST BE DECIDED DURING THE PRESENT CONSULTATIONS. HE SAID THAT HIS SIDE HAD ALREADY MADE CLEAR THEIR VIEW THAT HUNGARY SHOULD NOT BE A DIRECT PARTICIPANTS, BUT THAT IF THE WEST INSISTED ON THE ROLE OF A DIRECT PARTICIPANT FOR HUNGARY, THEN HUNGARY WOULD BE PREPARED TO ACCEPT THIS ROLE IF ITALY WOULD ALSO. AS WAS WELL KNOWN, ANY EFFORTS TO INCLUDE HUNGARY ALONE, WITHOUT ITALY BEING INVOLVED IN THE SAME MEASURES AND TO THE SAME DEGREE, WOULD NOT BE ACCEPTABLE TO HIS SIDE. EFFORTS TO THIS EFFECT BY THE WEST WOULD IN FACT BE AN ATTEMPT TO GAIN UNILATERAL ADVANTAGE AND WOULD RUN COUNTER TO THE PRINCIPAL OF NO DIMINUTION TO THE SECURITY OF ANY PARTY. HUNGARY AND ITALY WERE BOTH COUNTRIES IN THE SOUTHERN FLANKS OF THEIR RESPECTIVE ALLIANCES.

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